



## Qualys Q4 FY2022 Earnings Prepared Remarks

**Foster City, Calif., – February 9, 2023** – Qualys, Inc. (NASDAQ: QLYS), a pioneer and leading provider of disruptive cloud-based IT, security, and compliance solutions, today announced financial results for the fourth quarter ended December 31, 2022.

### **Blair King, Investor Relations**

Good afternoon and welcome to Qualys' fourth quarter 2022 earnings call.

Joining me today to discuss our results are Sumedh Thakar, our president and CEO, and Joo Mi Kim, our CFO. Before we get started, I would like to remind you that our remarks today will include forward-looking statements that generally relate to future events or our future financial or operating performance. Actual results may differ materially from these statements. Factors that could cause results to differ materially are set forth in today's press release and our filings with the SEC, including our latest Form 10-Q and 10-K. Any forward-looking statements that we make on this call are based on assumptions as of today, and we undertake no obligation to update these statements as a result of new information or future events.

During this call, we will present both GAAP and non-GAAP financial measures. A reconciliation of GAAP to non-GAAP measures is included in today's earnings press release. As a reminder, the press release, prepared remarks, and investor presentation are available on the Investor Relations section of our website. With that, I'd like to turn the call over to Sumedh.

### **Sumedh Thakar, president and CEO**

Thanks, Blair, and welcome, everyone, to our fourth quarter earnings call. We delivered another quarter of strong financial performance; reflecting a year of accelerated revenue growth and industry-leading profitability.

### **Product Innovation**

In terms of innovation, 2022 was a strong year for Qualys as we expanded our platform and our market opportunity. We introduced Context XDR to enable high-fidelity detection and response capabilities for our customers. We released VMDR 2.0 with TruRisk to enable comprehensive risk scoring and ITSM integrations. We brought External Attack Surface Management into our CyberSecurity Asset Management application. We unified multiple context vectors around asset criticality, vulnerabilities and system misconfigurations with asset telemetry in a single agent and brought a unique EDR application to market. Further flexing the power of our platform, we introduced our cloud-native TotalCloud with FlexScan, which pairs agent and agentless zero-touch assessment options with comprehensive cloud posture management and container security. These innovations allow our customers to reduce complexity as they standardize on a trusted platform that delivers an immediate ROI and lower total cost of ownership relative to siloed and traditional detection only technologies.

With CISOs increasingly focused on comprehensive risk management, we have upgraded our TruRisk platform capability to ingest third-party scans into the Qualys Cloud Platform, which we call Enterprise TruRisk Management and is now in preview with customers. Regardless of which vendor scans an organization's environment, with this enhancement to our TruRisk application, Qualys is now providing enterprise customers with a holistic, enterprise-wide risk score based on asset criticality and our Cloud Threat database, which is a unified threat intelligence platform of over 25 threat feeds. What makes this capability so special is our ability to then reduce an organization's enterprise risk score by leveraging Qualys' remediation applications with automated workflows through a unified dashboard.

Additionally, TotalCloud, which is our cloud-native risk management solution for public clouds, is now GA, and since our acquisition of Blue Hexagon in October, we've already added a new Cloud Detection and Response (CDR) module to our TotalCloud solution. As organizations increasingly prioritize moving workloads to hybrid and multi-cloud environments, we view this new ML/AI-based technology for zero-day threat hunting and response as another strong competitive differentiator in a rapidly evolving market. Looking forward, we will continue to seek out opportunistic acquisitions to further enhance our platform, accelerate our time to market and further expand our market opportunity.

### **Go-to-Market Initiatives**

Now turning to our sales and marketing execution, in Q4, we continued to witness organizations broadly responding to the evolving macro by applying additional layers of scrutiny to spend and delaying project start dates. We believe that with this increased scrutiny comes increased opportunity as organizations standardize on trusted platforms to consolidate security stacks, leverage automation, and achieve expedient remediation of risk. Qualys has a unique, organically built platform to address this need. Nevertheless, to fully capitalize on this opportunity requires crisp go-to-market execution. Over the last year, while we've made some meaningful progress on several fronts in this regard, including successfully growing the sales and marketing team and investing in our sales enablement and operations functions, we still have work to do in our sales execution. This is particularly evident within the context of today's market dynamics and persistent macro headwinds, which resulted in lower-than-expected bookings growth in Q4.

Accordingly, I'd like to share a couple of planned personnel and alignment changes within our sales and marketing organization, which position us for forward success. Earlier today, we announced the upcoming departure of our Chief Revenue Officer, Allan Peters. We thank Allan for his contributions during his tenure at Qualys as we continued to grow and scale our sales organization. In the interim, I will be overseeing the sales team as we focus on product-led growth, inherent in Qualys. We're fortunate to have a talented next-level team of regional sales leaders who are energized by our competitive position in the market, and I'm confident in our ability to effectively drive our business forward as we search for Allan's successor.

Additionally, I'm pleased to announce Pinkesh Shah, who joined Qualys in November of last year, was recently promoted to serve as our new Chief Product Officer, overseeing both Product as well as Marketing. Given Pinkesh's strong background in product-led growth, we believe having both product and marketing under the same leadership will help increase return on our investments and drive operational efficiencies in our go-to-market motion. It's great to have Pinkesh on the team, and we're looking forward to his leadership in helping execute our long-

term growth agenda.

As we diligently address the challenges brought on by today's market uncertainty, we remain confident in our long-term strategy and trajectory. I've met with over a hundred CISOs over the past few months, and their message is clear; they are looking to pivot to a platform-based solution to solve their complex security problems. In the face of an evolving macro, escalated threat environment and cybersecurity skills gap, organizations need to reduce complexity and costs while presenting measurable risk reduction initiatives to Boards and C-level executives.

This was underscored at our recent Qualys Security Conference in Las Vegas, which brought together over 500 Qualys customers and partners. Several customers in attendance highlighted the ability to measure their organizations' security posture by leveraging the Qualys Cloud Platform, while reducing risk and costs. One customer stated that through Vulnerability Management, Detection and Response (VMDR<sup>®</sup>) with TruRisk, they reduced risk and eliminated 60% of critical vulnerabilities in a very short amount of time without having to buy separate threat intelligence feeds.

Against this backdrop, there were several positives in Q4. We continued to see the steady adoption of VMDR, which is now deployed by 48% of our customers worldwide. A few key seven-figure VMDR wins in the quarter included two Global 500 financial institutions who chose Qualys for its ability to replace traditional siloed security tools and enhance security posture on a unified platform, and a Global 50 insurance company that is leveraging VMDR to not only detect, but also remediate vulnerabilities in both on-prem environments and cloud workloads.

Beyond these wins, I'll take a moment now to share a couple of additional successes with customers who are consolidating their security stacks to optimize spend and reduce risk.

First, a new logo Fortune 1000 web hosting company selected CyberSecurity Asset Management, VMDR, and our Custom Assessment and Remediation application in a seven-figure competitive win, replacing point solutions from three vendors with one platform. The ability for this customer to significantly enhance its security program with automated scripting, comprehensive internal and external asset criticality, quick remediation, CMDB sync and alerting on a natively integrated platform were all key differentiators compared to vulnerability detection only solutions in the market.

In addition, in 2022, highlighting organizations' strategic focus on high quality real-time Asset Inventory, we expanded our engagement with an existing financial services customer, signing over a \$800 thousand upsell deal for Qualys' CyberSecurity Asset Management solution. This customer is standardizing on our CyberSecurity Asset Management solution due to the rich asset context, End-of-Life visibility and real-time inventory they are able to get out of the same agents and platform they have already deployed for VMDR. This enabled them to enhance their investment in Qualys' platform by consolidating solutions, which is important to customers in current macro environment.

As more and more customers are beginning to perceive Qualys as a leading security platform that they can leverage to solve their complex and difficult security problems, we are growing increasingly confident in our ability to drive growth and gain market share. This is evidenced by the continued growth in our large customer spend with customers spending \$500,000 or more with us growing to 160 in Q4, up 27% from a year ago.

Turning now to our growth initiatives in the SME/SMB market, where we've witnessed slower growth, we've introduced new product packages: VMDR TruRisk, VMDR TruRisk FixIT with Patch Management, and VMDR TruRisk ProtectIt with both Patch Management and Multi-Vector EDR. These new packages offer simple, easy-to-deploy, all-inclusive cybersecurity solutions to manage, remediate, and protect against continuously emerging cyber threats and reduce risk. We believe that the convenient packaging and pricing of these offerings will help streamline the sales process for partners, reducing time to value, and further advance our value proposition in the SME/SMB market.

In addition, we're pleased to share that in Q4, we expanded our partnership with Oracle. Oracle Cloud Infrastructure (OCI) began offering a fully managed vulnerability scanning service that enables Qualys customers to leverage their vulnerability management licenses to scan their OCI Compute virtual machines. I'm also pleased to note OCI has selected Qualys' vulnerability management solution to help scan their internal environments for vulnerabilities. This is a testament to the effectiveness of Qualys in securing cloud infrastructure and advancing our partner ecosystem.

Finally, I'm pleased to announce that Qualys recently received FedRAMP Ready status at the High impact level on our newly introduced Gov-Cloud platform. Currently this is the only FedRAMP high ready platform offering inventory, vulnerability management and patch management in single unified workflow. With government agencies increasingly moving workloads from on-prem environments to the cloud, this marks the achievement of a key milestone and makes Qualys the only modern alternative to legacy scanners for federal, local and state government agencies. Given this certification, our consolidated platform and our investments to establish a public sector presence, we believe we're now well positioned to address a new vertical that could help drive growth in the long-term.

In summary, the cybersecurity market is a mission-critical technology. We believe our natively-integrated platform, that is quantifying, remediating and reducing risk, brings a highly differentiated value proposition to our customers as they get more security using less resources out of a single Qualys Cloud Platform. In 2023, we'll continue our disruptive innovation and further enhance and advance our go-to-market investments to crisply execute our long-term strategic vision with an already proven approach to balanced growth and profitability.

With that, I'll turn the call over to Joo Mi to further discuss our fourth quarter results and outlook for the first quarter and full year 2023.

### **Joo Mi Kim, Chief Financial Officer**

Thanks, Sumedh, and good afternoon. Before I start, I'd like to note that, except for revenue, all financial figures are non-GAAP and growth rates are based on comparisons to the prior year period, unless stated otherwise.

2022 was another notable year of product innovation for Qualys as we continued our product leadership while growing revenues by 19%, maintaining our gross margin at 81% despite inflationary pressures, and generating EBITDA margin of 45%. While our profit margin was well above our industry peers, 2022 was a year of investment for Qualys with both R&D and S&M growing faster than revenues. In R&D, we invested in our security research and product management teams to further strengthen the value proposition of our products and assist in executing our go-to-market strategy. In S&M, it was a mix of investments in headcount as well

as trade shows and marketing campaigns. Having executed against our 2022 investment plan with over a 20% increase in sales and marketing headcount, we look forward to optimizing our investments in 2023 as we remain committed to driving long-term profitable growth.

Now, let's turn to fourth quarter results. Revenues in the fourth quarter grew 19% to \$130.8 million, up from 16% in the year ago period. This includes a de minimis add from the Blue Hexagon acquisition, which contributed a few hundred thousand dollars to Q4 revenues. Revenues from channel partners grew 22%, outpacing direct, which grew 17%. Our revenue contribution mix has shifted slightly over the last year with direct making up 58% of total revenues vs. 59% a year ago. We expect a similar trend to continue in 2023. By geo, growth in the US of 19% was in-line with our international business, which grew 20%. Looking ahead to 2023, we expect our US and international revenue mix to remain at roughly 60% and 40%, respectively.

In Q4, we saw continued strength in customer dollar retention but lower performance in upsell with our net dollar expansion rate on a constant currency basis at 109%, down from 111% last quarter but up from 108% last year. Where we saw room for improvement was primarily in smaller customers who spent less than \$25,000 with us during the last year. We expect this segment to gain momentum with the launch of the new product packages that Sumedh just mentioned. In comparison, customers who spent \$25,000 or more with us increased by approximately 20% both in count and revenue.

In terms of new product contribution to bookings, we continued to see healthy demand for Patch Management and CyberSecurity Asset Management with the two combined making up 9% of LTM bookings and 15% of LTM new bookings in Q4. The increased adoption for these products resulted in 50% growth in Q4 on a combined basis.

Adjusted EBITDA for the fourth quarter of 2022 was \$55.1 million, representing a 42% margin, compared to a 45% margin a year ago. Operating expenses in Q4 increased by 25% to \$58.4 million, primarily driven by the growth in S&M investments, including higher headcount and related costs as well as spend on trade shows. EPS for the fourth quarter of 2022 was \$1.01, and our free cash flow for the fourth quarter of 2022 was \$40.9 million, representing a 31% margin, compared to a 32% margin a year ago. In Q4, we continued to invest the cash we generated from operations back into Qualys, including \$3.0 million on capital expenditures and \$104.5 million to repurchase 848 thousand of our outstanding shares. As of the end of the quarter, we had \$154.5 million remaining in our share repurchase program. We are pleased to announce that our Board has authorized an additional \$100.0 million share repurchase program, bringing the total available amount for share repurchases to \$254.5 million.

Now, let us turn to our 2023 guidance. Starting with revenues: For the full year 2023, our revenue guidance is \$553.0 million to \$557.0 million, which represents a growth rate of 13% to 14%. For the first quarter of 2023, we expect revenues to be in the range of \$130.2 million to \$131.0 million, representing a growth rate of 15% to 16%. This guidance is assuming no material revenue contribution from our newer products such as Context XDR and TotalCloud and continued unfavorable market dynamics throughout 2023, similar to what we witnessed in the fourth quarter of 2022.

Given the growth opportunities ahead of us, we will continue to invest in operations, people and systems while recognizing the importance of optimization. As a result, we expect full year 2023 EBITDA margin to be in the low 40%s, roughly in line with the fourth quarter 2022 margins. We

expect full year EPS to be in the range of \$4.10 and \$4.18 and for the first quarter of 2023, in the range of \$0.95 and \$0.97. Our planned capital expenditures in 2023 is expected to be in the range of \$18 to \$25 million and for the first quarter of 2023, in the range of \$4 to \$5 million.

In 2023, we plan to align our product and marketing investments to focus on specific initiatives to drive more pipeline and support sales in response to the current macro conditions, while at the same time maintaining a disciplined approach to unit economics. Throughout 2022, we accelerated the pace of hiring and brought in great talent across all functions of the company, increasing the total employee base by 18% while growing sales and marketing headcount by 22%. While we plan to continue to invest in 2023, given the environment we're in, we're planning to prioritize increase in investments on sales and marketing as well as related support functions and systems while largely maintaining our level of investments in engineering. As we shift to sharpen our execution by focusing on sales and marketing enablement and productivity, we believe we will be able to drive wallet share and long-term returns while balancing growth and profitability.

In conclusion, in 2022, we delivered strong top line growth and industry-leading profitability. We continued to lead with product innovation, introducing Context XDR and TotalCloud and adding TruRisk to VMDR. With these achievements, we remain confident in our ability to deliver on our growth opportunity long-term, and we will continue to prioritize investments critical to advancing our platform and go-to-market scale with a commitment to further elevate the areas of our business within our control and maximize shareholder value.

With that, Sumedh and I would be happy to answer any of your questions.